United Nations DP/2009/5

Executive Board of the
United Nations Development
Programme and of the
United Nations Population Fund

Distr.: General
5 December 2008

Original: English

**First regular session 2009**
19 to 22 January 2009, New York
Item 4 of the provisional agenda
**Recommendations of the Board of Auditors**

# UNDP: Report on the implementation of the recommendations of the Board of Auditors, 2006-2007*

## Report of the Administrator

*Summary*

The United Nations Board of Auditors, in its audit report A/63/5/Add.1, awarded UNDP an 'unqualified' audit opinion for the biennium ended 31 December 2007. This reaffirms the strategic thrust of UNDP efforts in addressing the three matters of emphasis and other audit concerns raised in the previous biennium. Pursuant to Executive Board decision 2007/10, the present report provides an implementation status update of the 82 audit recommendations made by the Board of Auditors for the biennium ended 31 December 2007. The present paper also reviews progress made (since the last update to the Board in January 2008) in addressing the Top 15 audit priorities in UNDP in 2006-2007 identified in its paper DP/2007/14 to the Board and outlines management plans in addressing the key audit priorities for the biennium 2008-2009, taking into account key the Board of Auditors Audit Report (A/63/5/Add.1), audit findings from the 2007 report of the Office of Audit and Investigations to the Executive Board (DP/2008/20), the Report of the Advisory Committee on Administrative and Budgetary Questions (A/63/474) to the General Assembly on the Concise Summary Report of the Board of Auditors (A/63/169), the guidance provided by the UNDP Audit Advisory Committee and the decisions of the Executive Board (DP/2008/13).

*Elements of a decision*

The Executive Board may wish to note (a) that the Board of Auditors issued an 'unqualified' audit opinion for UNDP with respect to the biennium ended 31 December 2007 and (b) recognize the progress made by UNDP in addressing the Top 15 audit priorities in 2006-2007. The Board may wish to express its support of specific management efforts in addressing key audit priorities in UNDP in 2008-2009.

* The compilation of data required to provide the Executive Board with the most current information has delayed submission of the present report.

08-63655 (E) 291208

## Introduction

1. For the biennium ended 31 December 2007, the United Nations Board of Auditors issued an 'unqualified' audit opinion on the UNDP financial statements (A/63/5/Add 1). UNDP was one of seven United Nations organizations (out of the 16 audited) to receive the 'unqualified' opinion. The significance of this lies in the fact that in the 2004-2005 biennium the Board of Auditors had issued a 'modified' audit opinion, where, among other concerns, there were three matters of emphasis, namely: audit management of nationally executed projects; bank reconciliations; and internal controls in the Atlas system. The recent positive result reaffirms the strategic thrust of many of the management initiatives implemented over past several years aimed at addressing the key audit findings of the Board of Auditors, as well as systemic issues underlying those findings.

2. The present report covers progress made (since the last update to the Executive Board at its first regular session 2008) in addressing the top 15 audit priorities in UNDP in 2006-2007. The audit was completed in May 2008, and by the date of this paper five audit recommendations had been implemented fully and another 70 partially implemented (implementation in progress). Together, those numbers represent 91 per cent of the recommendations.

3. On the basis of progress made, and recognizing remaining challenges, the present report outlines management plans to address key audit priorities for the 2008-2009 biennium, taking into account the report of the Board of Auditors (A/63/5/Add.1); the report of the Advisory Committee on Administrative and Budgetary Questions (A/63/474) to the General Assembly on the concise summary report of the Board of Auditors (A/63/169); key audit findings from the 2007 report of the Office of Audit and Investigations (DP/2008/20); and the guidance provided by the UNDP Audit Advisory Committee and the decisions of the Executive Board (DP/2008/13).

## I. Major observations and key recommendations of the United Nations Board of Auditors for the biennium ended 31 December 2007

4. While the core business areas (financial, procurement, human resources and programmatic management) audited in the 2006-2007 biennium remain fairly consistent with those of previous biennia, the audit report for the biennium (A/63/5/Add.1) signalled important shifts in the expectations of the Board of Auditors and its added focus on specific areas in UNDP. Specifically, UNDP noted the following:

(a) *Higher expectations in country office and headquarters bank reconciliations, and the management of advances to nationally executed projects.* The bar has been raised by the Board of Auditors. While recognizing "improvements in the management of bank reconciliations and the enterprise resource planning system, as well as UNDP management efforts to address concerns over nationally executed expenditure", as noted in Chapter 2 of its report, the Board of Auditors has challenged UNDP to achieve even higher standards for the new biennium in several keys areas. For example, in paragraph 357, the Board of Auditors recommends that UNDP closely monitor advances to nationally

executed projects provided to government and non-government organizations that have been outstanding for more than six months (instead of those greater than 12 months). As monthly bank reconciliation becomes a regular practice in many UNDP country offices, paragraph 214 recommends attention to unrecorded payments and unrecorded deposits in the external tables in bank reconciliation processes. Further, instead of using estimates for the computation of leave accrual liabilities, paragraph 173 recommends that UNDP should further leverage the Atlas system to compute accrued annual leave and repatriation grants liabilities for the financial statements. In response, UNDP has enhanced its Atlas 'financial dashboard' to track the status of external bank reconciliations and is the process of enhancing its Atlas aging report to better track advances to nationally executed projects outstanding for more than six months.

(b) *National capacity-building and inter-organization coordination.* In paragraph 430, the Board of Auditors indicates that it will focus on reviewing the implementation of the harmonized approach to cash transfers in country offices. This is one of the key components of national capacity building that will enable UNDP to work with programme governments to choose the most appropriate support modality to mitigate fiduciary risks and build sustainable capacity. This is also in line with General Assembly resolution 62/208, which calls upon United Nations organizations to adopt measures that ensure sustainability in capacity-building and to use national execution expertise as the norm in implementing projects. In response, UNDP will focus on supporting country offices facing difficulties in the implementation of the harmonized approach to cash transfers in their countries. So far, 13 countries are fully compliant with the harmonized approach, and many others are partially compliant. UNDP and UNFPA have advocated for and supported the adoption of the harmonized approach by the specialized agencies, funds and programmes, including its implementation in the 'delivering as one' pilot countries In addition, UNDP is working with Executive Committee partners and the United Nations Secretariat to revise the Financial Regulations and Rules so as to facilitate participation in direct budget support and other pooled-funding arrangements at the country level. The changes approved by the Executive Board during its second regular session 2008 have enabled UNDP to engage in direct budget support, thus responding to the call to support the development of national capacity for various modalities of development financing. Within established limits, and based on agreement with partners, UNDP is now able to pool funds in core mandate areas when this modality is in use.

(c) *Organizational risks and challenges associated with the planned implementation of the international public sector accounting standards.* At a more systemic level, the Board of Auditors has reiterated several key United Nations system-wide issues that need to be addressed in anticipation of the adoption of the international public sector accounting standards. Key emphases, reiterated in its concise summary report to the General Assembly (A/63/169), include (i) funding and recording of after-service health insurance liabilities on the face of the financial statements; (ii) the need to improve the quality and accuracy of non-expendable assets and to formalize project asset management policy in a manner consistent with the international public sector accounting standards; and (iii) the need to prepare the organization for the transition to the standards.

5. Besides working closely with the United Nations Secretariat and other United Nations organizations to harmonize accounting policies, financial regulations and rules, UNDP has developed a comprehensive change management and communication plan, targeting different stakeholders, senior management and staff, on the expected effect that adoption of the international public sector accounting standards will have on business processes and the changes to the financial statements that it will bring about. An organizational impact analysis of all UNDP country offices is under way to fine-tune the change management strategy of the organization as it professionalizes key functions and ensures specialization around the new business processes to be introduced under the international public sector accounting standards. UNDP will continue with its financial training certification programme to strengthen capacity in UNDP offices. UNDP will roll out regional accounting service teams, providing a number of small UNDP country offices with access to pooled expert resources in financial management in accordance with the standards.

6. With respect to after-service health insurance, UNDP agrees with the Board of Auditors that the full liability should be recorded on the face of the financial statements. UNDP will do this, effective 2010, as part of the implementation of international public sector accounting standards. In connection with non-expendable assets, UNDP has formalized its asset management guidelines while updating its internal control framework, and is conducting a half-yearly asset verification exercise in preparation for the interim audit of the 2008-2009 biennium. The exercise has yielded encouraging results, with a more than 96 per cent certification rate for the year 2008. This is expected to ensure better-quality asset data and reduce last-minute asset corrections at the end of the year.

## II. Current implementation status and plans to fully implement audit recommendations for the biennium ended 31 December 2007

7. As at 31 October 2008, five audit recommendations were fully implemented and another 70 recommendations partially implemented (implementation in progress). Together, those numbers represent 91 per cent of the recommendations. UNDP is targeting full implementation of at least 80 per cent of the 82 recommendations by the fourth quarter of 2009 and the remaining recommendations by the second quarter of 2010, in time for the closing of accounts for the 2008-2009 biennium (see table below).

**Implementation status by priority and target completion date**

| Priority | Fully Implemented (a) | Partially implemented (b) | Not implemented (c) | Total (a) to (c) |
|---|---|---|---|---|
| | | | | |
| High | 5 | 32 | 1 | 38 |
| Medium | 0 | 38 | 6 | 44 |
| Low | 0 | 0 | 0 | 0 |
| **Total** | 5 | 70 | 7 | 82 |
| **Percentage of total** | 6% | 85% | 9% | 100% |
| | 91% | | 9% | 10% |

8. The implementation schedule for several audit recommendations took into consideration the implementation plan of the recently approved UNDP human resources strategy and the UNDP information management strategy for 2008-2011. The UNDP procurement strategy is being finalized. It will cover such issues as the implementation of succession planning; mandatory procurement planning; and mandatory professional certification for key procurement staff. Audit recommendations that relate to the interim closing of the 2008 financial accounts are expected to be fully implemented by the second quarter of 2009 with the stabilization of the newly upgraded Atlas system in early 2009. This will include such matters as inter-organization accounts reconciliations; balance sheet accounts reconciliations and clean up, and asset verifications.

9. Due to several parallel activities during the period, a substantial number of recommendations are not expected to be fully implemented until the fourth quarter of 2009. These include (a) preparatory work on adoption of the international public sector accounting standards by UNDP in 2010, such as the formalization of project asset policy; a reassessment of field accommodation reserves; and mitigation of the risk associated with the transition to the standards; (b) the monitoring of inactive trust funds, the implementation of the common service programme, and support to country offices in the implementation of the harmonized approach to cash transfer modality; and (c) year-end events such as the reviews of outstanding advances to nationally executed projects and operationally closed projects.

10. A number of recommendations are expected to be fully implemented by the second quarter of 2010 to coincide with the finalization of the UNDP financial statements for the 2008-2009 biennium. These include the recording of after-service health insurance liabilities, the calculation of leave accrual liabilities, and a reassessment of field accommodation reserves.

11. As in the previous biennium, UNDP has started, since the issuance of the final Board of Auditors audit report (A/63/5/Add. 1), to set target completion dates for the 82 recommendations it contained (including 38 high- and 44 medium-priority recommendations). In the spirit of accountability, the division and the manager responsible for full implementation are provided on the 'audit tracking dashboard'. This is in line with General Assembly resolution 62/223 for greater accountability with respect to the implementation of audit recommendations. In 2006-2007, UNDP has established a system of periodic management review of the top 15 audit priorities (described in DP/2007/14) at Operations Group meetings, chaired by the Associate Administrator, and at quarterly reviews with the regional bureaux.

12. In line with the recommendation of the Advisory Committee on Administrative and Budgetary Questions (A/63/474), UNDP is consulting with the Board of Auditors to establish procedures for validating the implementation of audit recommendations and specific completion standards to verify that recommendations have been implemented fully. This is particularly important for recommendations that are of an ongoing nature, where full implementation would be dependent on parties outside UNDP, or where full implementation is expected to spread over multiple time periods.

# III. Progress made in addressing the top 15 audit priorities and action plan to address key and remaining risks

13. Pursuant to Executive Board decisions 2007/29 and 2007/10, UNDP took specific measures, during the 2006-2007 biennium, to address the top 15 audit priorities in UNDP, including the three matters of emphasis highlighted by the Board of Auditors.

14. Key actions taken by UNDP include a strong, visible commitment from the Administrator, the Associate Administrator and the directors of the regional and headquarters bureaux to address audit and analyse systemic issues associated with those recommendations. UNDP has also leveraged the half-yearly report of the Office of Audit and Investigation (OAI) to the Operations Group to proactively address audit risks identified through country office and headquarters audits. In addition, UNDP has institutionalized regular management review of strategic initiatives and progress made in addressing the top 15 audit priorities at the Operations Group meeting chaired by the Associate Administrator.

15. UNDP has also invested in longer-term solutions, such as staff professional certification programmes in the five core business areas of UNDP, and has piloted the implementation of regional shared services accounting teams as a way to build sustainable capacity over the long term for offices where staff capacity is limited (whether temporarily or permanently). In formalizing its top 15 audit priorities, UNDP has been able to operationalize its audit accountability and responsibility matrix through the quarterly review of financial and audit matters with the regional bureaux and use of the Atlas 'financial dashboard' to take targeted action on audit issues at the earliest possible moment.

## A. Significant progress made in the 2006-2007 biennium

16. *Improved management of fiduciary risks associated with nationally executed projects and audit results.* The total net impact of financial audit qualifications of nationally executed projects in 2007 was significantly reduced from $24.1 million in 2005 (1.5 per cent of total expenditure on nationally executed projects) to $5.15 million in 2007 (0.3 per cent of total expenditure). An 'aging report' has been implemented to better track the aging of advances forwarded to governments and non-governmental organizations for nationally executed projects. This has enabled UNDP to reduce its long-outstanding (more than 12 months) advances to nationally executed projects, from a net of $29.3 million in 2005 to $15 million in 2007. With the implementation of the risk-based approach to planning for audits of nationally executed projects, started in 2007, the percentage of audit reports on nationally executed projects received by the time of the audit improved from 74 per cent in 2005 to 96 per cent in 2007. The number of nationally executed projects with 'adverse' or 'disclaimer' audit opinions in 2007 dropped to 19 projects (out of a total of 1,004 projects), compared to 37 'adverse' or 'disclaimer' audit opinions in 2005, with reduced net financial impacts associated with these audit opinions.

17. *All headquarters and country office bank accounts are reconciled, a task which is now performed regularly.* All 67 bank accounts at headquarters and 553 in country offices were reconciled in time for the 2006-2007 biennium, compared with 258 outstanding bank reconciliations involving 49 country offices for the audit covering the 2004-2005 biennium. The special task force team mission has been useful in providing targeted support to country offices that faced difficulties with bank reconciliations. In addition, for a handful of offices with limited staff capacity, the bank

reconciliations were temporarily performed centrally, at the Office of Finance and Administration of the Bureau of Management.

18. *Key risks have been mitigated with enhanced internal controls in Atlas and exception transaction monitoring in place.* UNDP enhanced the internal controls in the Atlas system with the roll-out of audit trail capabilities in 2006, permitting the tracking of changes to vendor records, bank accounts and foreign exchange documents. UNDP also implemented a security question feature for forgotten password requests to prevent unauthorized access to Atlas, and implemented an industry-tested oversight system to track potentially questionable transactions in Atlas and infringement of internal control framework guidelines.

19. *A truly global financial and human resources management system covers all UNDP offices, including UNDP Brazil.* With the migration of UNDP Brazil human and financial resources management to Atlas in early 2008, UNDP achieved a truly global enterprise resource planning system. Since the migration of human resources and payroll management for international professional staff from the 'legacy' Integrated Management Information System to the Atlas system in 2008, UNDP now has a truly global workforce system that will enable it to deliver on its human resources strategy for talent management and succession planning.

## B. Action plans to address key and remaining audit risks in the 2008-2009 biennium

20. The review that was undertaken in consultation with OAI indicated that improvements were noted in eight of the 15 priority areas. This means that the initiatives started are having their desired effect, though it does not necessarily mean that the matter has been completely resolved. There is a need for continuing attention and focus on the areas identified below, which are either potentially key risks or contain residual risks that need to be addressed in the 2008-2009 biennium (see annex).

*Management of audits of nationally executed projects*

21. Notwithstanding progress made, the management of audits of nationally executed projects remains a top audit priority in UNDP. UNDP will ensure the timely submission of these audit reports and audit follow-up plans, and to strengthen controls of advances to nationally executed projects outstanding for more than six months, as recommended by the Board of Auditors. In addition, through the Development Operations and Coordination Office and working collaboratively with the regional bureaux, UNDP will assist country offices having difficulty implementing the harmonized approach to cash transfers.

22. While national capacity building will remain the central objective of our programmatic interventions, alternative payment modalities could be pursued with programme governments (such as direct payments), as required to mitigate fiduciary risks while building national capacity in financial management. UNDP is in the process of enhancing its Atlas reporting capability to enable better aging analysis of advances older than six months to nationally executed projects. Except with special approval from the Associate Administrator through the regional directors, no new advances to nationally executed projects would be disbursed until those outstanding for more than 12 months have been resolved. UNDP has made the management of audits of nationally executed projects a performance indicator on the UNDP 'executive scorecard' for country offices.

*Project quality assurance*

23. In line with our programmatic accountability to the Executive Board and to programme governments to build the required capacity and contribute to national development priorities, UNDP will step up efforts in project monitoring, improving mechanisms for project design, and ensuring regular project appraisal.. Project risk management is an integral part of the larger enterprise risk management strategy for UNDP to deliver on commitments made in its strategic plan, 2008-2011.This is also in line with the guidance provided by the UNDP Audit Advisory Committee.

24. UNDP will leverage its recently enhanced results-based management system to provide a more effective process for the planning, monitoring and reporting of key results areas across UNDP offices. Specific attention will be given to identifying SMART indicators and in the prompt financial closure of operationally closed projects in line with the recommendations of the Board of Auditors.

*Procurement management at country offices*

25. In response to concerns raised by OAI and the Board of Auditors, UNDP will (as part of its procurement strategy) be taking special efforts to strengthen procurement capacity and competency of the contracts and assets procurement committees in country offices. While the UNDP procurement certification programme is recognized within the United Nations as a 'best practice' and an avenue to building competency and professionalism, UNDP is working towards ensuring that every UNDP office has at least one procurement-certified buyer.

26. As part of its procurement strategy, UNDP is establishing procurement planning processes in country offices and at headquarters. UNDP will also link delegation of procurement authority to mandatory procurement planning, demonstrated capacity and performance. UNDP expects to roll out an on-line e-tool in 2009 to help business units link planned procurement to risk and value considerations. With targeted training at regional procurement workshops and the eventual placement of all five regional chief procurement officers, UNDP expects to improve the quality of procurement submission to the Advisory Committee on Procurement regionally and at headquarters, and to implement periodic review and analysis of the different types of waivers requested and approved by the Committee.

*Atlas user access management and internal control*

27. To mitigate risks and strengthen internal controls in the Atlas system, UNDP has formalized its usage and security policies for information and communications technology in its programme and operations policies and procedures. Atlas user access and user accounts are being streamlined to better manage inactive Atlas user accounts. User access profiles will be streamlined in accordance with the revised guidelines for the internal control framework to incorporate controls for other key business processes in Atlas.

28. The chief information security officer at UNDP is working with the Office of Finance and Administration and Office of Human Resources to conduct regular reviews of Atlas security systems. UNDP will continue to improve its industry-proven oversight system by expanding its monitoring and reporting capabilities with respect to irregular and inconsistent transactions and potential frauds in other business processes.

29. *External tables in monthly bank reconciliations*. While monthly bank reconciliation is becoming regular practice in country offices, the UNDP Audit Advisory Committee and the Board of Auditors have recommended additional attention to unrecorded payments and unrecorded deposits in the external tables in

bank reconciliation processes. These are primarily payments made outside the Atlas system, which could be a source of fraud or abuse. UNDP has started to track these external items in the Atlas 'financial dashboard', which will be reviewed with the regional bureaux at quarterly meetings.

30. *Asset management*. UNDP has formalized its asset management guidelines as part of its update of the internal control framework, and will conduct its half-yearly asset verification exercise in preparation for the interim audit of the biennium 2008-2009. This has yielded encouraging results, with a better than 96 per cent certification rate. This is expected to ensure higher-quality asset data and to reduce last-minute asset corrections at the end of the year. As the Board of Auditors, recommended, UNDP will dispose unserviceable assets and formalize its policy for the proper recording and management of project assets in accordance with the requirements of the requirements of the international public sector accounting standards.

*Management of trust funds*

31. In line with the directives of the UNDP Audit Advisory Committee and the Board of Auditors, specific attention will be given to the management of trust funds in 2008-2009. At the end of the 2006-2007 biennium, 93 of the 647 UNDP trust funds (or 14 per cent) showed deficits totalling $14.8 million. Deficits in trust funds funded by the European Commission continue to be a concern. While such deficits may be due to foreign exchange losses as a result of factors such as pre-financing activities from UNDP dollar reserves and limitations in fully hedge payments, further attention may be required.

32. UNDP will focus closely on enhancing the management and oversight of multi-donor trust funds. Revisions to standard legal agreements (the memorandum of understanding and the standard administrative arrangement) were drafted to be used for establishing multi-donor trust funds and joint programmes using the pass-through fund management option.

33. *Integrity of staff recruitment processes* UNDP is formalizing its recruitment regulatory framework to clarify the responsibility and accountability of hiring managers and to reinforce prescribed recruitment policies and guidelines. This is a part of the recently-approved UNDP human resources strategy. UNDP will continue to use its on-line job vacancy tracking tool for oversight monitoring, and will build on field work undertaken by the Office of Audit and Investigations to address instances of non-compliance, lack of underlying capacity, or other issues highlighted by the audits.

## IV. Conclusion

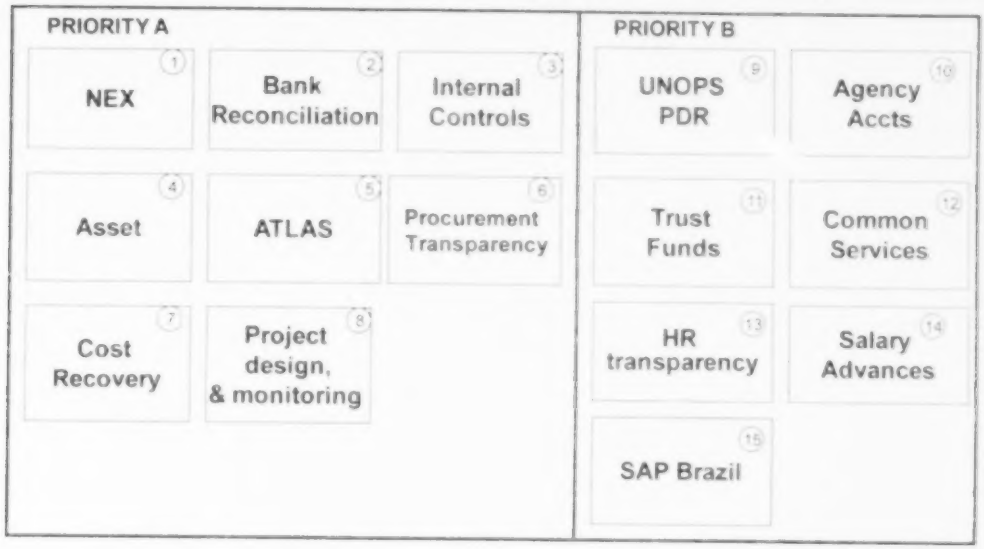
34. UNDP is committed to strengthening accountability and organizational responsiveness to audit recommendations within its overall accountability system. UNDP is revising its top 15 audit priorities to better reflect remaining risk and new or emerging risks highlighted by the Board of Auditors. They will also reflect the guidance provided by the UNDP Audit Advisory Committee in managing the change associated with the implementation of the International Public Sector Accounting Standards and that of the Executive Board, especially with audit recommendations that remain unresolved for longer than 18 months.

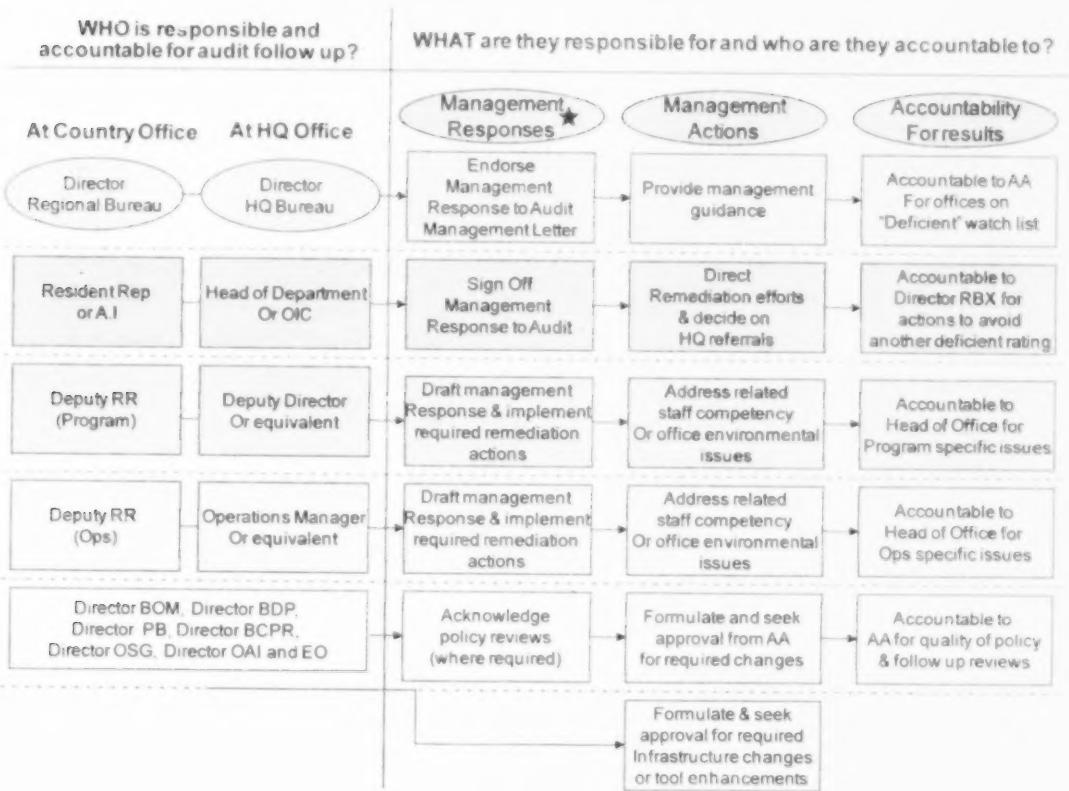
35. UNDP has made significant progress in addressing its top 15 audit priorities of 2006-2007. This reflects the significant investment made in implementing specific management strategies over the last 3-4 years, and has meant that UNDP is

maturing in its approach to audit management. This being so, it is envisaged that UNDP will now move towards having a 'top 10' audit priorities for 2008-2009.

36. UNDP will invest further in capacity-building and professionalization programmes for its staff, and will develop alternative, more sustainable measures, such as the regional shared services teams to support bank reconciliations and other core business areas. While the award of an 'unqualified' audit opinion by the United Nations Board of Auditors for the biennium 2006-2007 affirms the strategic thrust of management interventions, UNDP intends to build on the progress made and prepare its stakeholders, management and staff for implementation of the international public sector accounting standards by 2010.

**Annex. Top 15 audit priorities in 2006-2007, and audit accountability framework**





WHO is responsible and accountable for audit follow up?
WHAT are they responsible for and who are they accountable to?
At Country Office
At HQ Office
Management Responses
Management Actions
Accountability For results
Director Regional Bureau
Director HQ Bureau
Endorse Management Response to Audit Management Letter
Provide management guidance
Accountable to AA For offices on "Deficient" watch list
Resident Rep or A.I
Head of Department Or OIC
Sign Off Management Response to Audit
Direct Remediation efforts & decide on HQ referrals
Accountable to Director RBX for actions to avoid another deficient rating
Deputy RR (Program)
Deputy Director Or equivalent
Draft management Response & implement required remediation actions
Address related staff competency Or office environmental issues
Accountable to Head of Office for Program specific issues
Deputy RR (Ops)
Operations Manager Or equivalent
Draft management Response & implement required remediation actions
Address related staff competency Or office environmental issues
Accountable to Head of Office for Ops specific issues
Director BOM, Director BDP, Director PB, Director BCPR, Director OSG, Director OAI and EO
Acknowledge policy reviews (where required)
Formulate and seek approval from AA for required changes
Accountable to AA for quality of policy & follow up reviews
Formulate & seek approval for required Infrastructure changes or tool enhancements